

## FLUID MINERALS BOND PROCESSING USER GUIDE

KeywordsXX BankruptcyA. Background

By law, the MMS cannot bill a bankrupt payor for prepetition debts. The BLM **can**, however, take action against a bankrupt debtor's bond since the bond is **not** considered part of the bankruptcy estate (refer to Solicitor's Opinion, No. BLM R.M. 0641, March 5, 1986). Both the BLM and MMS must be aware of procedural limitations and requirements from a legal standpoint in order to comply with the Bankruptcy Code and still ensure collection of maximum available amounts under the bond.

BANKRUPTCY  
PROVISIONS

This section provides only general guidance regarding the areas of bankruptcy proceedings that concern the BLM and MMS operations. Various bankruptcy courts interpret the Bankruptcy Code sections differently. Therefore, the same result cannot be expected in each proceeding. Accordingly, coordination among the BLM, MMS, and the appropriate Department of the Interior Solicitor's Office is necessary to protect the U.S. Government in bankruptcy proceedings.

Pursuant to the 1978 United States Bankruptcy Code (11 U.S.C. 101 et seq.), a debtor, typically an individual or a company experiencing financial difficulties, may seek an organized liquidation of its debts and business or a restructuring of the debt through a reorganization. A Chapter 7 bankruptcy proceeding is a liquidation process in which the assets of the debtor are sold and the creditors are paid a pro rata share from the proceeds. Generally, the percentage of the debt returned to the creditor in a Chapter 7 proceeding ranges from zero to 4 percent. The bankruptcy court appoints a trustee in a Chapter 7 proceeding who is responsible for conducting the business of the debtor's estate during the liquidation procedure.

CHAPTER 7  
BANKRUPTCY

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KeywordsCHAPTER 11  
BANKRUPTCY

The Chapter 11 bankruptcy proceeding generally provides for the orderly restructuring of the debts of the business to allow the debtor to continue to operate with the assets necessary to conduct business after its discharge from the bankruptcy proceedings. The plan of reorganization, which establishes the method of restructuring the debt, allows for some return to the creditors while at the same time enabling the debtor to continue to operate. In a Chapter 11 proceeding, the court may appoint a trustee to supervise the business affairs of the entity, or the debtor may be allowed by the court to operate its financial affairs and business as a debtor-in-possession.

Included by the debtor in the filing of the bankruptcy petition is a list of scheduled creditors to whom prepetition amounts are owed. This list is a part of the bankruptcy schedules. Generally, an agency's (e.g., the MMS's or BLM's) scheduled amount or its claim is an unsecured debt. Although the agency may be listed with a scheduled amount, the agency needs to verify the amount and file a proof of claim for the prepetition amount through its designated representative (through the appropriate Solicitor's Office) before the "bar date" established by court order. The "bar date" is the last date set by the court to receive and to allow proofs of claim filed by creditors. The proof of claim can be amended with less difficulty than a scheduled amount can be changed.

Upon receipt of notification of the filing of a bankruptcy petition by a debtor, the BLM and MMS need to notify the designated bankruptcy coordinator of the other agency so that the leases held by the lessee are reviewed for defaults and that the financial account status of a payor is reviewed for prepetition and post-petition amounts that may be owed. If an agency discovers a bankruptcy proceeding for which it is **not** receiving notification by the bankruptcy court, but in which it believes it has an interest, it is to contact the appropriate Solicitor's Office to request preparation of an agency notice of appearance in the bankruptcy proceeding.

ACTION UPON  
NOTIFICATION  
OF BANKRUPTCY  
OF AN ENTITY

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Keywords

Currently, the MMS produces a quarterly listing that shows entities involved with the Federal mineral leasing program that have filed bankruptcy petitions. This updated listing is circulated throughout the MMS and to all BLM State Offices. Upon discovery of defaults on the leases, possible refund amounts, or prepetition receivables, the appropriate Solicitor's Office is to be notified by memorandum with the necessary documentation attached. The Solicitor's Office coordinates with the BLM State Offices and the MMS concerning presentment of proofs of claim and other bankruptcy problems. It is important that no action against the bond of the bankrupt entity be taken by the BLM without concurrence of the Solicitor handling the proceeding. Although the bond, which is provided by the entity to the U.S. as assurance that the lease obligations will be fulfilled, is **not** part of the estate of the bankrupt entity and remains available to the BLM for restoration of the bankrupt party's leases for purposes of protection of health, safety, and the environment, the BLM office needs to advise the Solicitor's Office prior to making a demand on such a bond held by a bankrupt entity.

BANKRUPTCY  
LISTING  
PREPARED  
BY MMS

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B. Agency Procedure Regarding Discrimination Against DebtorKeywords

Any Federal agency policy that treats debtors in a substantially different manner because of the bankruptcy proceeding violates the Bankruptcy Code prohibition concerning discrimination against a debtor, 11 U.S.C. 525, which states:

DISCRIMINATION  
OF FIRM DUE TO  
BANKRUPTCY  
PROHIBITED

" . . . [A] governmental unit may not deny, revoke, suspend, or refuse to renew a license, permit, charter, franchise, or other similar grant to, condition such a grant to, discriminate with respect to such a grant against . . . a person that is or has been a debtor under this title . . . or another person with whom such bankrupt or debtor has been associated, solely because such bankrupt or debtor is or has been a debtor under this title . . . has been insolvent before the commencement of the case . . . or has not paid a debt that is dischargeable . . . ."

Accordingly, agency lease cancellation solely by virtue of the bankruptcy is prohibited. However, a lease may terminate by its terms during the course of the bankruptcy proceeding, e.g., a nonproducing lease may terminate automatically for failure to pay annual rental. Pending lease offers and applications for approval of assignments are to be reviewed and processed in the normal method, unless notification is received from the bankrupt party or the court to withhold the approval of assignments transferring the bankrupt interests. If other reasons exist for rejection of the pending actions and the agency cannot grant approval, before acting, the agency is to consult with the appropriate Solicitor.

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C. Automatic StaysKeywords

Upon the filing of a petition under either Chapter 7 or Chapter 11, the automatic stay provisions of 11 U.S.C. 362(a) become effective. The stay prevents "the commencement or continuation . . . of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the [bankruptcy] case;" the enforcement of a judgment obtained against the debtor before the commencement of the bankruptcy case; the taking of any other action "to collect, assess, or recover a claim against the debtor that arose before the commencement of the [bankruptcy] case," and the "setoff of any debt owed to the debtor that arose before the commencement of the [bankruptcy] case against any claim against the debtor."

AUTOMATIC STAY

The automatic stay is applicable against all entities, including agencies of the U.S. Government. This provision was implemented to ensure that the bankruptcy is an orderly process and to safeguard the assets of the bankrupt estate.

Exceptions to the automatic stay have been interpreted narrowly by the courts. Generally, any exercise of a regulatory power to protect a purely pecuniary interest of the United States would be considered a violation of the stay. Exercise of power to protect the public health, safety, and welfare would come within the exceptions.

1. Operator in Bankruptcy

If a default occurs, the BLM can proceed regardless of whether the default occurred before or after the bankruptcy action was filed. The automatic stay provision does not apply where a governmental unit is suing (or otherwise proceeding against) a debtor to prevent or stop a violation of fraud, environmental protection, consumer protection, safety, or similar police or regulatory enforcement laws, or attempting to fix damages for violations of such a law. Therefore, as long as the BLM's action is not simply seeking to protect the pecuniary interest of the U.S., the BLM may enforce the regulations and issue notices of incidents of noncompliance pursuant to the normal time frames for infractions that occurred prior to the bankruptcy filing. Penalties and assessments or fines and damage calculations may be made. However, actual collection of money may not be allowed because enforcement of a money judgment would give the U.S. a preferential treatment to the detriment of other creditors.

LEASE OPERATOR  
IN BANKRUPTCY

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Keywords

The automatic stay provisions do **not** apply to defaults that arise after the filing of the bankruptcy action. The BLM is to continue to enforce the regulations against the operator, i.e., remedial action may be sought. Normal time frames may be employed for correction of both prepetition and postpetition violations of operational requirements. Additionally, assessments and penalties or fines and damage calculations may be made. Actual collection of money might not be allowed by the bankruptcy court, however.

AUTOMATIC STAY  
NOT APPLICABLE  
TO SOME DEFAULTS  
AFTER FILING OF  
BANKRUPTCY

If you have knowledge that a lease operator is in bankruptcy and may result in lease operational problems, notify the lessee by a copy of any notification that is sent to the operator to allow the lessee to respond, since the lessee is also responsible for compliance with all lease terms and conditions.

The operator's bond is a source of payment for defaults since the bankruptcy filing has no effect on the bond proffered to the BLM for lease operations. It is important that the BLM follow the required regulatory procedures and give prompt notification of all operational infractions using the notice of incidence of noncompliance and written orders, particularly if lease shutdown or cancellation has to be sought.

## 2. Lessee is the Debtor

LESSEE IN  
BANKRUPTCY

Remedies available if the lessee is conducting oil and gas operations are the same as when an operator is in charge. The automatic stay provisions will generally **not** prevent enforcement actions. Lease cancellation may not always be allowed, however. Additional considerations exist since the lease is an executory contract that may be either accepted or rejected by the bankrupt lessee. The 1984 amendments to the bankruptcy laws require the assumption or rejection of a lease within 60 days after the date of the bankruptcy filing for both a Chapter 7 and Chapter 11 bankruptcy, otherwise the lease is deemed to be rejected by the bankrupt party. The BLM must establish whether the lease is in default and what actions are necessary to cure such default. This would primarily include incidents of noncompliance. Failure to pay rent timely is **not** considered a default because the lease automatically terminates by its own terms. Such termination is **not** precluded by the automatic stay. Likewise, since failure to pay rent terminates the lease, the ability to continue or reject the lease is no longer an option for the debtor.

LEASE TERMINATION  
FOR FAILURE TO  
PAY ANNUAL RENTAL  
NOT PRECLUDED BY  
AUTOMATIC STAY

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Keywords

If the lessee decides to reject the lease rather than accept it, in essence, a lease relinquishment occurs. The BLM can file a claim for damages that would relate back to the date of the bankruptcy filing. Such a claim must involve safety, health, and environmental conditions related to the lease operations (see Appendix 22 for a Solicitor's Memorandum BLM.ER.0645, dated May 19, 1987).

BANKRUPTCY  
REJECTION CAUSES  
LEASE TO BE  
RELINQUISHED

The imposition of an assessment to compel compliance with the regulations implementing the Mineral Leasing Act is an exercise of the Department's regulatory power which is not stayed by the filing of a bankruptcy petition by an oil and gas lessee or operator (see Chase Energy, Inc., 115 IBLA 76 (1990)). It is proper for the BLM to issue a written order directing clean up of oil-contaminated soil from a well site.

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D Procedures for Collecting Prepetition Debts Under BankruptcyKeywords

1. The bankruptcy coordinator for the MMS, Office of the Associate Director for RMP, compiles a list of all known bankruptcy filings, including the name of the debtor, type of proceeding, and date of bankruptcy filing. This list normally is compiled on a quarterly basis with any updates transmitted during the interim period. Each BLM State Office receives a copy of this bankruptcy list directly from the MMS.

PREPETITION  
DEBT  
COLLECTION  
PROCEDURES

2. Based on the bankruptcy list received from MMS, the SO fluid leasing adjudication is to take the following steps:

a. Order an ALMRS Proprietor's Report to determine those leases held by each entity listed on the bankruptcy list;

b. Check the leases indicated for each entity on the ALMRS Proprietor's Report against the biweekly MMS Delinquent Lease Account listing;

c. Request reclamation reports from the Field Office Fluid Mineral Operations staff for those leases listed on the ALMRS Proprietor's Report. The Field Office is to immediately advise the SO Adjudication of any claims against the bankrupt party, including an itemization of any outstanding assessments and penalties.

d. Report all defaults identified on leases held or operated by any of the bankrupt entities to the appropriate Solicitor's Office.

3. When any notices or other written documentation of bankruptcy filings that are **not** included on the MMS bankruptcy listing are received by any BLM office, the SO Bankruptcy Coordinator is to immediately notify the MMS Bankruptcy Coordinator (MS 660, Denver) and the appropriate Solicitor. Copies of all other pertinent information, including whether the BLM has identified a default, also is to be transmitted to the appropriate Solicitor's Office.

BANKRUPT FIRMS  
NOT INCLUDED  
ON MMS LISTING

4. Based on any notification of bankruptcy filings from the BLM, the MMS will:

a. Identify whether the debtor is a payor to the MMS. If so, the MMS will determine if the debtor has outstanding royalty-related obligations and will determine the amounts owed.



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Keywords

b. Report all prepetition receivables to the Office of the Solicitor, Rocky Mountain Region.

5. The BLM and MMS must notify one another to consolidate debts for demand against the bond of a bankrupt entity. The appropriate Solicitor is informed by both the MMS and BLM of the planned action against the bond, but no action against the bond is to be taken without concurrence from the Solicitor.

SOLICITOR'S  
CONCURRENCE  
TO MAKE DEMAND  
AGAINST BOND OF  
BANKRUPT ENTITY

6. The BLM SO Fluid Leasing Adjudication is to take the lead to demand payment under the bond.

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E. Procedures for Collecting Postpetition Debts Under BankruptcyKeywords

Debt collection procedures for postpetition claims and amounts are the same as the procedures to be used for nonbankrupt entities. The only exception is that, if debts are not paid in full by the payor, lessee/operator, or corporate surety, the case is referred to the appropriate Solicitor for action.

POST-PETITION  
DEBT  
COLLECTION  
PROCEDURES

NOTE: The above information is taken from the joint BLM-MMS report entitled Collection Under Bonds of Royalty-related Obligations for Onshore Fluid Mineral Leases, prepared by the Fluid Bonding Task Group, April 1988. Refer to that report for additional, more detailed information on this subject.

JOINT BLM-MMS  
TASK FORCE REPORT  
OF APRIL 1988